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## **Yugoslavia (FRY)**

### **Tobacco and Products**

## **Tobacco Industry in Yugoslavia - Update 2001**

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Report Highlights: Economic troubles have led to a substantial decline in raw tobacco production in Yugoslavia to roughly half of 1980 levels or 9,2000MT (MY2001 est.). However, demand for cigarettes exceeds local supply. Finished cigarette imports of 6,700 billion pieces are forecast for CY2001. Total FRY cigarette consumption is estimated at 20 billion cigarettes annually. Note: All totals here apply to Serbia, Montenegro and Kosovo combined (i.e. FRY), unless otherwise stated.

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Includes PSD changes: No

Includes Trade Matrix: No

Unscheduled Report

Sofia [BU1], YI

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## **Overall Economic Crisis Hits Tobacco Production and Cigarette Demand**

The overall economic problems of Yugoslavia – due to 10 years of relative isolation - have negatively affected the tobacco industry. Low cigarette prices, a shortage of raw material imports and inputs have made cigarette production less profitable. One problem hurting both raw tobacco and cigarette production is the uneven transition of tobacco enterprises from state to private ownership. Unclear ownership laws continue to inhibit investment and reduce efficiencies in the tobacco industry, especially on the manufacturing side.

### **Raw Tobacco Production**

Raw tobacco production is flat. The old (Milosevic) government called for an increase in MY2000 tobacco production by 30 percent, but this forecast was not fulfilled due to the regional drought. Estimated tobacco production in MY2001 is 9,200 MT or roughly the same level as the past three years. Yugoslavia produces burley (50 percent of total crop); virginia (25 percent) and oriental (25 percent) tobacco. Previous government schemes focused on increasing virginia-type tobacco production and currently exports of virginia tobacco are prohibited. Oriental tobacco for blending is also in short supply due to smaller domestic crops. However, neighboring Balkan countries provide Yugoslavia with much of its oriental tobacco needs.

The government has gradually increased the amount of support to the tobacco producers and manufacturers in hopes of reviving a hard currency export industry. The policies included increasing government set ceiling prices; production subsidies and favorable credits for purchases of equipment and inputs -- especially fertilizer which would boost yields.

The Yugoslav Tobacco Industry Association had forecast a MY2000 production increase to the 12,500 MT level. However, regional drought conditions reduced yields to an all time low of 9,200 MT despite overall stable area planted. Only a small portion of the tobacco crop is irrigated (in South Serbia/Moravia). Yields and quality in that area were good last year. The largest MY2000 losses were found in Vojvodina in the virginia and burley crops. The average sized farm for burley production is 4 hectares (HA), but for virginia-type production, farms average 0.5 HA. Expansion in MY2001 was seen in increased area planted in only the Srem region of Serbia.

### **Cigarette Production**

In MY2000, Yugoslav cigarette production was estimated at 13,400 billion cigarettes which is about 65 percent of domestic use requirements. This production level is 10 percent lower when compared to 1998 (14,700 billion cigarettes). Cigarette prices in Yugoslavia are some of the lowest in Europe. Data from December 1999 shows that the cheapest domestic cigarette cost 9 dinars, and the most expensive cost 17 dinars or between \$.04 and \$.25 per cigarette at 1999 exchange rates. After the political changes in the country in late 2000, cigarettes prices jumped by almost 50 percent. But in dollar terms, cigarette prices have fallen across the board versus last year.

<b>Retail Prices of Cigarettes on Serbian Market</b>			
Type	December 1999	October 2000	June 2001
Local and imported	9-17 Din/pack	15-35 Din/pack	25-40 din/pack
Serbian/ Montenegrin	NA	NA	15-35 Din/pack
Macedonian	NA	NA	15-30 Din/pack
Slovenian/Croatian	NA	NA	25-30 Din/pack
West European/ U.S.	NA	NA	60-135 Din/pack
Note: The exchange rate in June 2001 is 66 Din per one U.S. dollar.			

Cigarette factories are forced to import a large portion of raw tobacco for blending as well as almost all other inputs. Given the low cigarette prices, profit margins in the manufacturing sector are almost zero. Factories are seeking to source the cheapest possible tobacco and inputs. Cigarette producers would like the government to increase prices, and to receive some support in order to make higher quality products.

## **Taxes**

Taxes on cigarettes are fairly low compared to Western Europe and average 40 percent of the retail price. There are several types of additional taxes such as a "check-off" tax of one dinar per pack of cigarettes which goes for subsidies for tobacco production. Relatively low taxes keep cigarette prices low. However, revenue in the budget is also reduced. Taxes on imported cigarettes are 30 percent of the total import price. Currently, the government has difficulties collecting taxes on imported cigarettes due to smuggling.

## **Cigarette Manufacturers**

There are four cigarette factories in Yugoslavia. Two of them are in Serbia (Nis and Vrania), one in Montenegro (Podgoritz), and one in Kosovo (Gniliane). The largest and most profitable manufacturing facility is in Nis with a capacity equal of the other combined. Currently, Nis and Vrania produce cigarettes for the domestic market in Serbia with a population of about 8 million people.

Total FRY cigarette consumption is estimated at 20 billion cigarettes annually. There are plans for building a new factory in Vojvodina to increase domestic manufacturing capacity and fill this shortage. In the past, Vojvodina used to have two cigarette factories, but they were closed in the 1980s due to oversupply on the Yugoslav market.

The factory in Gniliane produces small quantities for the Kosovo market. The factory in Podgoritz

used to produce about 3-4 billion cigarettes annually. Currently, production is highly reduced due to the lack of export markets. The market inside Montenegro is very small and exceeds the output of the factory in Podgoritza. Since 1996, Serbia established special customs points for checking illegal imports of cigarettes due to smuggling concerns and in order to collect all due taxes.

## **Privatization**

Many industry observers believe the state tobacco factories should be privatized. Currently, the law allows a foreign buyer to purchase a maximum of 49 percent of shares while the state holds 51 percent. However, unclear ownership and confusing privatization legislation has discouraged outside investors.

Recently, some large European companies have expressed an interest in buying the cigarette factory in Nis. To date, however, unclear ownership issues, high number of employees and problems in privatization legislation discouraged potential investors. The cigarette factory in Podgoritza was "privatized" several years ago when 46 percent of shares were sold to small share holders, mainly managers of the factory. The remaining shares are still "state" property.

There are two plans for new cigarette facilities. The first one is a project of Serbian government, according to which a new cigarette factory should be built in Kragujevac at the previous location of an automobile company "Zastava". The other project is for an investment of the Croatian cigarette factory "Ronhil" Rovinj to build a cigarette factory in Novi Sad (Vojvodina). At present, it is not clear how both investment plans could proceed.